

Business and management
Standard level
Paper 2

Thursday 21 May 2015 (morning)

1 hour 45 minutes

Instructions to candidates

- Do not open this examination paper until instructed to do so.
- Section A: answer one question.
- Section B: answer two questions.
- A calculator is required for this examination paper.
- A clean copy of the **business and management formulae sheet** is required for this examination paper.
- The maximum mark for this examination paper is **[60 marks]**.

Section A

Answer **one** question from this section.

1. Nzuri Kio (NK)

Nzuri Kio (NK) is a company that manufactures products made of glass, such as windows and table tops. *NK* sells its products in its own regional trading bloc, a group of eight countries that all have developing economies. *NK* is located in a poor country where the national government is not very efficient and public sector services are limited. The country's infrastructure needs investment, and quality of life is low. At school, students are in very big classes, with over sixty students in each; few students complete middle school.

The manager of *NK* is considering purchasing new, high-quality equipment for its factory: glass-making machines from *Carrucci SpA*. *Carrucci SpA* is an Italian company that makes the best glass manufacturing equipment in the world. Its computerized equipment is innovative and very efficient. Glass can be cut perfectly, with almost no waste. However, the equipment is expensive and requires highly skilled workers. The new equipment would lead to a better product, which should result in higher sales and a higher gross profit margin.

The total cost of the equipment is \$800 000. *NK* is considering two different sources of finance:

- (Option A) a seven-year \$720 000 bank loan.
- (Option B) selling \$800 000 in shares.

Financial information for *NK*, for the year ending 31 May 2014:

Cash	\$176 000
Cost of goods sold	\$3 900 000
Creditors	\$230 000
Debtors	\$674 000
Expenses	\$3 800 000
Interest	\$120 000
Loan capital	X
Net fixed assets	\$2 600 000
Retained profit	\$970 000
Share capital	\$300 000
Sales revenue	\$8 200 000
Short-term borrowing	\$270 000
Stock	\$320 000
Tax	\$70 000

(This question continues on the following page)

(Question 1 continued)

- (a) Using a PEST framework, describe **two** external factors that may affect *NK*. [4]
- (b) Using data from the table:
 - (i) calculate loan capital X (*show all your working*); [2]
 - (ii) construct a fully labelled balance sheet for *NK*; [4]
 - (iii) calculate *NK*'s gross profit margin (*no working required*); [1]
 - (iv) calculate *NK*'s forecasted gearing ratio for **Option A** and for **Option B** (*show all your working*). [4]
- (c) Examine the **disadvantages** of **Option A** and of **Option B** as sources of finance for the purchase of the new equipment. [5]

Turn over

2. Exploration Toys (ET)

Exploration Toys (ET) manufactures educational toys. Dr Berac Loïc set up the business in 2006. *ET*'s unique selling point (USP) is that its toys are not only safe and fun, but also teach children to explore and solve problems. *ET* sells directly to consumers online, business-to-customers (B2C), and relies only on word-of-mouth promotion*. *ET* set its toy prices higher than those of its competitors.

Table 1: selected data for *ET*, for 2014.

Sales revenue	€300 000
Number of toys sold	12 500
Fixed costs	€121 800
Variable cost per toy	€10

By 2014, sales had stopped growing. A marketing consultant told Berac that with only word-of-mouth and B2C e-commerce sales, the situation would not improve. She recommended that *ET* restructure its marketing mix to include more promotion, lower prices, and an additional sales method called “toy parties”. *ET* would need to recruit part-time sales associates (representatives) to host the toy parties. At the parties parents could see the toys and children could play with them. The sales associates would sell *ET*'s toys on a commission-only basis.

However, if sales grew significantly *ET* would need to lease a larger factory, which would increase fixed costs. Berac forecasted financial data based on the marketing consultant's recommendations.

Table 2: forecasted financial data for *ET*, for 2015.

Cash sales revenue	€352 000
Closing cash balance at year-end 2014	€37 000
Fixed assets	€40 000
Fixed costs	€180 000
Raw materials	€128 000
Sales commissions	€32 000
Other variable costs	€32 000

* word-of-mouth promotion: information passing from one person to another or others through oral communication

(This question continues on the following page)

(Question 2 continued)

- (a) Describe *ET*'s current distribution channel and the channel recommended by the marketing consultant. [4]

- (b) (i) Using **Table 1**, calculate *ET*'s net profit margin for 2014 (*show all your working*). [2]

- (ii) Using **Table 2**, calculate *ET*'s forecasted net profit margin for 2015 (*show all your working*). [2]

- (iii) Comment on the change in net profit margin from 2014 (actual) and 2015 (forecasted). [3]

- (c) Using relevant data from **Table 2**, prepare an **annual** cash-flow forecast for *ET*, for 2015. [4]

- (d) Examine **two** reasons why *ET* originally charged higher prices for its toys than those charged by its competitors. [5]

Turn over

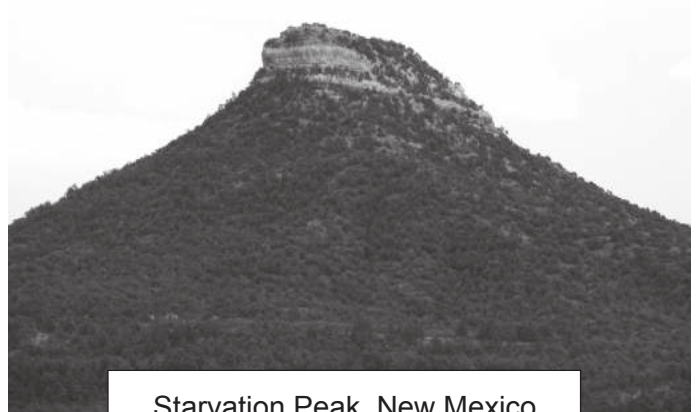
Section B

Answer **two** questions from this section.

3. Starvation Peak Running Shoes (SP)

Starvation Peak Running Shoes (SP) is a shop that sells running shoes in Santa Fe, New Mexico, United States (US). Its name comes from the local mountain called "Starvation Peak".

SP customers can buy running shoes at a lower price online, but *SP* has a unique selling point (USP) concerning its vision and its local reputation. *SP*'s vision statement is: "Running sustains life, locally and globally".



SP is very well known locally, as they support the local running community in the Santa Fe area. They do so in several ways by:

- sponsoring "running days" at schools
- giving discounts to children and students
- offering "running clinics", where *SP* employees help people improve their running techniques
- organizing races and other local events.

The biggest event organized by *SP* is its annual "Race to the Top" on Starvation Peak. According to a local legend, a tribe of Native Americans forced enemies up to the peak, where they died of hunger (starvation). *SP* promotes the event with the slogan: "Running sustains life, even on Starvation Peak". "Race to the Top" has been popular for ten years. However, there are now conflicts between stakeholders. Local businesses like the event, as it attracts tourists to the area. One pressure group, however, argues that it portrays Native Americans in a negative way. Another pressure group argues that the event damages the natural environment of the mountain. The local authorities managing Starvation Peak have been asked to refuse permission for *SP*'s "Race to the Top".

[Source: © International Baccalaureate Organization 2015]

- (a) Describe **one** type of below the line promotion that *SP* may use to promote its "running clinics". [2]
- (b) Explain **two** reasons why *SP* supports the local running community. [6]
- (c) Analyse the role of *SP*'s vision statement. [5]
- (d) Advise the local authorities as to whether permission for *SP*'s "Race to the Top" should be refused. [7]

4. The significance of changes in international labour mobility

Though the global population may grow from 7 billion in 2011 to 7.6 billion by 2020, many countries will experience a decline in the number of working-age people. Already in Japan and Europe, each year more people retire from the workforce than young people enter it. By 2020, this problem will also affect Russia, Canada and China. Other countries such as India, Brazil and Indonesia have young populations and young workforces.

Unfortunately, many people lack the skills that employers need. A recent study found that 31 % of employers worldwide struggle to fill jobs requiring basic skills. 65 % of multinational companies have difficulty recruiting new employees with advanced skills. In emerging economies the problem is worse. Difficulties in meeting operational objectives of recruitment prevent many companies from meeting their strategic objectives.

Companies are responding by recruiting new employees from other countries. This practice is called “expanded recruitment”. It has led to more international labour mobility, diverse workforces within companies, and diversity in global cities.

Supporters of expanded recruitment argue that the labour problem is demographic: the best solution is to make labour mobility easier. Furthermore, diversity both within companies and in society should improve international understanding and will increase creativity. Critics of expanded recruitment argue that it does not solve the real problem: many jobs require advanced skills, and most educational systems have not responded to those needs. Expanded recruitment has also created other issues for companies, such as problems in communication.

Expanded recruitment has also led to some anger in countries and local communities not accustomed to large immigrant populations.

[Source: adapted from <http://www.ey.com>
Used with permission.]

- (a) Identify **one** opportunity and **one** constraint for companies caused by demographic change. [2]
- (b) Comment on **one** potential communication problem for a company with a diverse international workforce. [2]
- (c) Explain the statement “difficulties in meeting operational objectives of recruitment prevent many companies from meeting their strategic objectives”. [4]
- (d) Analyse **one** strategy that a global company could adopt for developing future human resources (you may refer to a global company that you have studied). [5]
- (e) Discuss the significance of changes in international labour mobility. [7]

Turn over

5. Coca-Cola India

The American company *Coca-Cola* is investing financially and strategically in India. Thirteen Indian businesses have received contracts to prepare and package *Coca-Cola* drinks across India. Over 7000 distributors and 2.2 million retailers, supermarkets and restaurants are selling *Coca-Cola* drinks. For *Coca-Cola*, success in India is an important part of the business's strategy, as India has a population of over 1 billion people. A question faced by *Coca-Cola* is whether it should use market development or market penetration strategies.

Coca-Cola India has a wide product portfolio including *Coca-Cola* and other brands such as *Limca* and *Sprite*. *Coca-Cola India* directly employs over 25 000 people and has created indirect employment for more than 150 000 people through its vast logistics, supply and distribution.

Coca-Cola India has recently piloted an online store for the growing e-commerce market through the website *Coke2Home.com*. The online store will provide consumers with an alternative channel to buy *Coca-Cola* drinks. Consumers can also learn about the full range of *Coca-Cola*'s drinks on the website and sign up to receive special promotions via email or mobile phone message.

Although the online store is working very well in some cities, there are still some difficulties:

- Because delivery costs are high, *Coke2Home.com* accepts only large orders such as for parties and celebrations.
- Many *Coca-Cola* retailers and supermarkets fear that *Coke2Home.com* will create a new form of competition.

[Source: adapted from <http://www.coca-colaindia.com/>
and S Sharma, (31 May 2013), *Mumbai Times Business, Times of India*]

- (a) Define the term *product portfolio*. [2]
- (b) (i) Draw and label all elements of the Ansoff matrix. [2]
- (ii) Explain **one** advantage and **one** disadvantage for *Coca-Cola* in India of using the Ansoff matrix as a decision-making tool. [4]
- (c) With reference to *Coca-Cola*, analyse the role played by multinational companies in the global business environment. [5]
- (d) Discuss the costs **and** benefits to *Coca-Cola India* of e-commerce. [7]